Universität ⬆ Siegen
Fachbereich 5 – Wirtschaftswissenschaften

International Monetary Economics
Final Exam

60 minutes
No documents allowed – non programmable calculator allowed

Dr Jean-Baptiste Desquilbet

1- [1 point] Define the "balance of payments" of an economy.
[2 points] Give the list and a short description of the accounts of the balance of payments.

2- [2 points] A country faces a surplus in the financial account of its balance of payments. What can you infer as to its relations with the rest of the world?

3- [3 points] Define the "uncovered interest parity" and state it, using the mathematical notations you find appropriate.
[1 point] In June 2006, the 3-month interest rate on the Euro is 2.94% and the 3-month interest rate on the US Dollar is 5.27%; According to the "uncovered interest parity", what can be inferred about the Euro-US Dollar exchange rate in the next three months?

4- [3 points] Define the Marshall-Lerner condition and state it, using the mathematical notations you find appropriate.

5- We represent a small open economy with fixed price (Keynesian unemployment) by the following 3 equations (stated as deviations from equilibrium):

(IS)	$sY = -nR + G - zY + Y_f + \theta Q$	goods market equilibrium
(LM)	$M = \lambda Y - \beta R$	money market equilibrium
(BP)	$-zY + Y_f + \theta Q + \varphi(R - R_f) = 0$	foreign currency market (BoP flow equilibrium)

Y = national income ; R = domestic interest rate ; Q = exchange rate (home currency price of the foreign currency) ; M = money supply ; G = government expenditures ; Y_f = foreign income ; R_f = foreign interest rate.
The parameters s, n, z, θ, λ, β, φ are positive constants.

   a- **[2 points]** What does the assumption that θ is positive mean?
   b- **[2 points]** We assume that $\varphi - z\beta/\lambda < 0$. Interpret this condition in terms of "international capital mobility".
   c- **[4 points]** Further assuming $Y_f = R_f = 0$ (foreign variables are constant), study the impact of a budgetary expansion (increase in government expenditures: G>0) on the equilibrium value of national income and the other two endogenous variables, according to the exchange rate regime (fixed or flexible): draw a graph for each exchange rate regime and give a short conclusion.

International Monetary Economics
Final Exam (2)

60 minutes
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Dr Jean-Baptiste Desquilbet

1- [1 point] Define the "balance of payments" of an economy.
[2 points] Give the list and a short description of the accounts of the balance of payments.

2- [2 points] A country faces a deficit in the financial account of its balance of payments. What can you infer as to its relations with the rest of the world?

3- [2 points] Define the "purchasing power parity" (PPP) and state it, using the mathematical notations you find appropriate.
[2 points] Give at least three reasons why the PPP theory does badly in explaining facts.

4- [3 points] Define the Marshall-Lerner condition and state it, using the mathematical notations you find appropriate.

5- We represent a small open economy with fixed price (Keynesian unemployment) by the following 3 equations (stated as deviations from equilibrium):

(IS) $sY = -nR + G - zY + Y_f + \theta Q$ goods market equilibrium
(LM) $M = \lambda Y - \beta R$ money market equilibrium
(BP) $-zY + Y_f + \theta Q + \varphi(R - R_f) = 0$ foreign currency market (BoP flow equilibrium)

Y = national income ; R = domestic interest rate ; Q = exchange rate (home currency price of the foreign currency) ; M = money supply ; G = government expenditures ; Y_f = foreign income ; R_f = foreign interest rate.
The parameters s, n, z, θ, λ, β, φ are positive constants.
We will assume that $Y_f = R_f = 0$ (foreign variables are constant).

a- **[1 point]** Explain which assumption can be interpreted as saying that the Marshall-Lerner condition is satisfied.
b- We assume that "international capital mobility" is "high".
    [1 point] Draw a graph representing the equilibrium of the economy.
    [2 points] Study the impact of a monetary expansion (increase in money supply: M>0) on the equilibrium value of national income, the interest rate and the exchange rate, in a flexible exchange rate regime.
    [1 point] Complete the graph drawn previously to illustrate these effects.
c- **[2 points]** Is there any role for monetary policy in a fixed exchange rate regime?
d- **[1 point]** What is referred to as the "incompatibility triangle"?

Maximum score: 20 points.